The Free Market

"If you don't create a free market, a black market will emerge"

NEWSLETTER OF THE LITHUANIAN FREE MARKET INSTITUTE - www.freema.org/Newsletter/index.phtml

NEWS

Conference on higher education

On November 5, 2002 in Vilnius, the Lithuanian Free Market Institute and the Knowledge Economy Forum will hold a conference "Lithuanian Higher Education: Diagnosis and Prognosis". The aim of the conference is to stir up debates on higher education policy in Lithuania in order to create an effective system of higher education, to improve the quality of higher education to reflect technological progress and market needs, and to establish qualitative, student- and market-oriented studies. At the event, LFMI will present the fundamentals of the proposed reform of education system.

Conference participants will discuss such topics as the impact of higher education on man's life and development, modern world challenges on higher education, and innovations of higher education reforms around the world. LFMI will present the fundamentals of the proposed reform of education system.

Among the speakers will be representatives from higher schools, student and business community, the President's Office, the Parliament, and the Ministry of Education as well as Lithuanian and foreign policy analysts.

The idea to organise this event was prompted by understanding that higher education is facing new challenges, its problems are aggravating and reforms conducted do far have brought futile results. All this encourages specialists and academia to assess directions of reforms anew and to encompass the aspects of both systemic management of studies and financing of the system as well as to propose directions which would reflect the modern realia and the expectations of society.

The conference is financed by the Freedom House and the Open Society Fund.

LFMI analyses housing financing policy

In summer and autumn LFMI placed a special focus on issues of housing conditions and abilities to improve the housing situation of people in Lithuania. Within the framework of a joint-project with the World Bank and the Housing and Urban Development Foundation, LFMI conducted the Lithuanian household survey. The aim of the survey was to analyse Lithuanian households' income and expenditure, expectations regarding changes in their economic situation, expenditure priorities, housing conditions, willingness and efforts to improve housing conditions as well as attitudes towards commercial loans and state housing policy. This data will serve a primary source of information in drafting the National Housing Strategy, so that its goals and forms of state support for housing correspond to the real situation in the country - people's financial abilities and expectations and budget abilities. The Strategy is to be drafted by the Government by the end of 2002.

Drawing on the results of this survey and seeking to halt lavish and ill-directed housing policy, LFMI is analysing the effectiveness of the housing policy pursued in Lithuania and the existing and proposed instruments of housing financing. In a round table discussion held in July, LFMI presented an in-depth study of the contract saving system (the so-called "Bausparkassen" system) to parliament members, financial analysts and specialists of housing policy. The study reveals the weaknesses of the contract saving system and is based on other countries' experience. In a press conference in September, LFMI's policy analysts pointed out this system's defects once again. If adopted, LFMI argued, this system will fail to achieve the goals of state support, as it is tailored to support middle- and higher-income people, not the poorest residents. Moreover, it would jeopardise the state finances, the financial sector and the competitiveness in the banking sector. LFMI's policy analysts also stressed that the adoption of the contract saving system would markedly reduce preconditions to introduce other housing finance systems, such as a mortgage lending system, that do not entail state support. A bill on mortgage lending system is being drafted at the moment.

International conference on taxes and competitiveness

On December 5-6, 2002 in Vilnius, the Lithuanian Free Market Institute, the Friedrich Naumann Foundation and the Heritage Foundation, in partnership with the *MG Baltic* and the *Philip Morris Lietuva,* will host a two-day international conference "Tax Competition and Competitiveness." The conference is also supported by the business daily *Verslo zinios* and the *PricewaterhouseCoopers.* The event is organized under the courtesy of President of Lithuania Valdas Adamkus.

The conference will examine the peculiarities of tax regimes and policy reforms pursued in the Baltic States and Russia and their impact on business, investment, and economic development. A special focus will be put on tax planning, its role in ensuring competitiveness, and the countries' policies towards tax heavens. The main facets of tax legislation in the

European Union will also be presented to analyse the issues of tax harmonization and tax competition.

The aim of the conference is to highlight different approaches to tax policy adopted by the countries and to answer the questions - how these countries will fare in terms of tax regimes and investment environments in the near future; what lessons Lithuania should draw from practice of other countries; and what challenges the EU should accept in order to provide favourable conditions for its countries to compete on the EU market and among themselves.

The audience of the conference will comprise approximately 120-150 participants, including members of parliament, high-ranking government officials, ministry executives, leading business people, policy analysts, representatives of international institutions, and academia from the Baltic States, Russia, and the EU countries.

More information about the event can be downloaded at LFMI's homepage www.freema.org/tax.phtml.

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FEATURE

In summer 2002, the United Nations held the World Summit on Sustainable Development in Johannesburg which addressed environment and policy issues. This meeting was an important driver of environmental policy globally in the coming decade. Seeking to join this major debate, LFMI presents its view on the principles of sustainable development.

What Are the Principles of Sustainable Development Meant For?

Guoda Steponaviciene, Vice President, LFMI

The discussion of any development strategy must clarify: 1) what is developed; 2) who develops; 3) in what way it is developed; and 4) what comes out of it. Let us see whether these statements, which have become nearly mandatory in a political discourse lately, indicate explicitly the object, subject and mode of action.

Although such type of rhetoric is not used directly, the context implies that the object of sustainable development means all activities of a man worldwide. It follows that the performer of such action is each individual. Global conferences and congresses on the above-mentioned topic mobilise all people for the achievement of common goals, namely eradication of poverty, pollution and other problems of mankind. The organisers of Johannesburg Summit also stress that "participation of all sectors is critical". Representatives of state institutions, social groups (youth, women, NGOs and scientists) and interest groups (trade unions, farmers) should convene and submit their proposals on how to expand sustainable activities and assume commitment to action. This action should be such as to prevent the impact of human activities on environment in the present and future alike.

The notion of sustainable development and particularly implementation thereof is rather obscure. And it's not just because the term "sustainable" may be translated into other languages (e.g. Lithuanian) as words with entirely different meanings. If we treat sustainable development in a wider sense, we arrive at a common human positive goal which is obvious to everyone: as many people as possible should live better. Every individual and community of individuals are striving for this goal and at least each democratic government should strive for this. Thus it looks as if no new object for the discussion remains.

But there exists a narrower treatment of the goal which, to put it simply, may be formulated as follows: how to make individuals who seek profit and other welfare take account of the so-called public interests. This has been vital since the cradle era of mankind. Therefore, all world religions have got their own ethics codes in which one of the imperatives is to love one's kin (or at least cause no damage to one), and folklore of the entire world is full of tales about the good "fool" who finally must get reward and of such proverbs as "don't foul the well, you may need its waters". With a whip and honey cake, didactics and rational reasoning, mankind is learning how to make its life better.

Such events as the global Johannesburg Summit, despite the goals of participation, are not yet geared toward an individual but toward an institution or organisation and particularly the states (the opposite is impossible practically). In this context business, profit-making corporations in particular, is identified as an opponent to sustainable development. Meanwhile, the objective of the new policy is the policy that would force company owners to adopt their decisions not only in view of their own interests but also the so-called public interests. This would be absolutely fine but there is one "but". Nobody, even a global congress properly representing all interest groups, knows and has methods to find out what "a public interest is." There is no need to hold the Summit to learn that everybody wants to live better but no-one can tell what decisions must be adopted for people, enterprises, and governments to make this happen. These decisions will differ depending on thousands of local geographical, cultural, political and other circumstances.

The Western civilisation has existed up to now on the basis of the rule how to build up that social welfare, which is to allow an individual achieve private goals and thus heed and meet the interests of people surrounding him. Only one small detail is needed for that, i.e. legally laid down conditions to seek this goal in accordance with property immunity and competition principles. Meanwhile, the principles of sustainable development read that man must adopt decisions in view of others' interests rather than his own. The situation grows similar to the task "go nobody-knows-where and fetch nobody-knows-what". The economic consequences of such wandering are weakened effectiveness of activities which, consequently, leads to slackened welfare, growing poverty, pollution and other evils. After all, it was in pursuit of their own welfare that people threw their creative powers at what we today call modern economy and technological progress, owing to which both poverty and pollution have incomparably decreased than, let's say, a century ago.

So we can come to the following conclusion. The conceptual framework of sustainable development is not practical. The general objectives raised therein are plain and understandable but the methods of achieving them do not lead to the goal. So it is small wonder that statements and declarations on this issue abound as hardly anything can be achieved without rhetoric. Unless separate individuals, who hadn't read fairy tales in their childhood and thus keep throwing litter into their neighbour's courtyard, are convinced that it's not the way to behave.

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FEATURE

When the parliament made public their plans on the introduction of the contractual savings system for housing in Lithuania (the so-called Bausparkassen system), LFMI launched an active public dissemination campaign explaining the system's faults and warning about deleterious effects it would have on the budget, the financial sector and the society in Lithuania. The following article was the first attempt in the printed press made to alert the public about the dangers of the system (printed in the weekly Veidas, July 4, 2002).

A Sad Tale of a Housing Bank

By Elena Leontjeva, Consultant, LFMI

Less than half a year has passed since the government abandoned its improper role of a banker, while attempts again are made to put it back where it was.

People have just started enjoying the first fruits of competition among banks, while plans are already being concocted to undermine it and to legalize privileges. Of course, no one calls for giving banks into the hands of the government or advocates against free competition. The changes are being orchestrated under a cover of nice banners carried by a crowd of respected and important people. But when one nice day these banners become a law, we will all be forced to carry them.

Questionable Saving

At first glance banners with the words "Helping People without Homes!" look attractive to everyone. After all, not every citizen in Lithuania yet may close a bank's door with a dreamed-of loan for housing, despite that competition among banks offers a unique variety of services and constantly falling interest rates. It's either the salary too low, or no money for the initial payment, or too many dependants in the family. Who will take care of all these people? That's why laws are drafted under which specialized housing, or Bauspar, banks will start operating along with commercial banks and will provide financing to those who are not able to take out loans in the market and who agree to save for themselves. This whole business will have to be subsidized by the government. However, just as you bring this banner down to the ground and feel it, you should sadly acknowledge that the privileged banks will undercut the competition in Lithuania's banking sector and cost a fortune to all taxpayers without realising the declared goal. Instead of being given a real opportunity to purchase a home of dreams, people will be embroiled in dubious long-term relationships with a privileged bank. Let me explain why.

Under the draft law, all those wishing to receive loans will first have to prove their thriftiness and solidarity. For two years in a row they will be obligated to put their earnings in a bank account until they accrue a specified amount, and only then they will be allowed to qualify for a housing loan. We are very well familiar with this principle of solidarity from the Russian folklore. Do you still remember the tale of the wolf, all frozen, hungry and beaten up by old village women, his tail torn off and stuck in a hole in the ice, who had the cunning and satiated fox sitting on his back and singing this song: "The unbeaten is riding the beaten!" Whatever nice words may one use to explain to people that they should contribute to the nation's savings plan and win the bank's trust, the essence remains the same: people who don't have money will not just be left without a housing loan but they will also be made to lend money to the one who has it – the bank. This is the first but not the only unpleasant surprise to people who are dreaming of purchasing an apartment or of building a house.

The second one is that the size of a loan is "tied" to the amount accumulated in a bank account. If an individual saves ten thousand litas over several years, he becomes eligible for a loan of the same size. But not for a larger amount, as the carefully drafted law restricts that. In other words, if an individual loans ten thousand litas to the bank, they will entrust exactly the same amount to him at the end of the savings period. However, such amount will be insufficient to buy an apartment, to say nothing of a house. Even if monthly earnings are rather considerable and an individual manages to save twice this size, the result will be disappointing all the same. Thousands of Czech residents have already become convinced of that, when after a fixed period of saving they eventually received the loans of their dreams. It became obvious that with such loans a saver had on average about 20 to 50 percent of residential property's price, the accrued amount in a bank account, interest and subsidies included. This means that he will have to keep looking for ways to buy an apartment. The situation is even more aggravated because an individual will have to mortgage his property to the Bauspar bank despite a meagre amount of the loan drawn from it. The law doesn't say what items an individual will have to offer to other creditors in order to earn their trust and get the missing part of financing.

Subsidies Spoil People

Certainly, there would be nothing wrong if a bank wished to create such a scheme of financing and had clients who trust it – this would be the matter of an agreement between them. Why was the law needed in this case? In order to legalize subsidies, which the government would have to pay to people for saving and interest rates paid by banks, lower than on the market. The bankers' argument that they will not gain anything from this is unjustified, because loans will be granted at lower interest rates than on the market. Even if the difference between interest received and interest paid is the same as when performing other banking operations, a bank will gain from this, as it will attract more clients by providing subsidies rather than competing in the market. Certainly, it may happen so that terms offered by banks competing in the market may be more favourable than those of the subsidized bank. The history bears witness to such cases. And yet, the mentality of "take when they give you" will encourage a number of clients to go to a place where something is given "for free". The subsidy is really considerable: twenty percent of the saved amount, but no more than five-hundred *litas* per year. Is this amount sufficient to attract quite a number of gullible people who would agree to be ridiculed and ripped off for this money?

The justifying argument is that the purpose of subsidies is to increase saving, "which is inadequately weak in Lithuania." This type of thinking poses a risk that some day we will hear such sayings as "Why should I get married, cook potato dumplings, weed my garden and bear children if the government does not subsidize me for this?" "If you want me to make a move, subsidize and pay for it." And what really makes me feel ashamed is to have to remind people, economists in particular, that in order to give a subsidy the government must get this money in the first place - either through taxes or in the form of a loan. This means that subsidized saving will increase at the expense of shrinking private funds, private borrowing and investments.

It is worth remembering the bizarre experience of the Czech people and other countries: individuals who didn't plan to purchase residential property kept their money in Bauspar banks just to get subsidies. After taking out the money together with a "free" gift from the taxpayers, they bought cars, had surgeries and went travelling around the world. As I mentioned before, the size of deposits is more suitable to buy such things than purchase a real residential property. Far-sighted Lithuanian politicians may boast that they have made trips abroad not in vain and that they have scrutinised the problem. That's why they propose paying subsidies only to those who would actually take mortgage loans. However, there's nothing to boast about here. Mending an unsound system does not make that system sounder, but it adds to the list of bad news. It means that a bank will successfully use the subsidy earmarked by the government each year until the time comes to issue a loan. However, many things may happen in between. For example, after overall calculations an individual may decide that taking a loan does not make any sense because it won't be enough to purchase an apartment, while he will have no other sources to borrow from (according to the statistics, most people will be confronted with this particular problem). Or an individual may search and find that he can get a larger and cheaper loan somewhere else. It may also happen that the bank itself will decide that someone does not qualify for its loan, for example, after a child birth in the family, or, putting it the red-tape way, families with the increased number of dependents, or if one of the spouses becomes disabled or if their earnings shrink. In all these cases an individual won't be able to get the promised and assigned subsidy, although he had kept his money in the bank at lower interest rates than on the market, thus giving the difference between them to the bank as a gift! One does not have to muse long to understand that after a long period of saving it will be lower-income people who will have lesser chances to obtain a loan, and this means that someone who was not beaten again will be riding on the back of someone who had been beaten badly.

The New Privileged

Not only a specialized bank may be eligible to the happy category of the "unbeaten". The law stipulates that an individual who has made a contract may obtain a loan prior to the prescribed minimal term of saving if, according to the distribution index, he falls into a specific group of clients. What an eldorado! While the unlucky ones will be painstakingly saving every penny and taking it to the bank, those from a special group of clients will be able to obtain loans right after signing a contract and not having had much time to accrue the required amount. The authors of the law may offer a lucid explanation that this grouping of clients is objective and designed to check their creditworthiness. Certainly, subjective evaluation does not become objective when squeezed into rigid indicators and formulas. The bank, all the same, will give a higher rating to a person with higher rather than lower income, with fewer rather than more children, i.e. dependents, and with a working rather than a disabled wife. This provides an open opportunity to discrimination against certain groups and legalizes favouritism. Moreover, an individual who takes out an early loan will also circumvent one of the system's most adverse restrictions, under which the size of the loan may not exceed the amount accrued in a bank account. Without having accumulated anything, he will get the total amount specified in the contract!

I can already hear reproaches that client grouping and issuing loans to more creditworthy people are ordinary market principles, and it's ridiculous to argue against them. Of course, it is natural to apply them to people who borrow in the market, but promotion of such principles seems immoral when a special institution is created to provide loans to those who are unable to borrow under market conditions. If the goal of the new system will be to correct market imperfections and to seek noble social aims, it has to be done consistently, while the market, which has been renounced once, has to be left outside this issue.

Upon realizing all this, one may sincerely wonder how someone dares propose such a defective model to Lithuania, especially when it's common knowledge that specialized Bauspar banks in other countries faced a complete fiasco and that some of them are undergoing liquidation or litigation? I guess it would be difficult for the government to give a reply. And there are even more difficult questions. Although housing lending in the market has strengthened, some other long-awaited moves have not been made yet, e.g. legalization of a variety of banking institutions and services and issuance of mortgage-backed securities. It is these moves that would pave the way for housing loans and make them considerably cheaper and not require any subsidies from the society. The only thing that needs to be done here is utilizing resources allocated for legislation in a consistent and wise manner. One needs to learn a lesson from the painful and deplorable experience in rallying a number of government institutions and their efforts for the project inspired by a private bank. A lot of scarce resources, the most important of them being time rather than money, have been wasted this way. To acknowledge the mistakes would be a significant and welcome action. However, to avoid future plans to compete through the government, someone from the Administration should announce loudly that the last state-owned bank in Lithuania has been privatized and that from now on the Lithuanian government will no longer engage in the role of a banker but rather take care of its legitimate and proper duty – the adoption of prudent regulations.

Certainly, one should remember the lessons from the folklore here. In the said tale, when asked by the wolf about the kind of song he was singing, the fox replied boldly: "The unbeaten is riding the beaten!" With a sad smile on his face, the wolf said: "That's true", and hastened his pace.

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ACTIVITIES

July – September 2002

Agricultural policy

In light of the ongoing discussion on the highly relevant issue for agriculture, i.e. decision on whether or not to fix a transitional period for sales of agricultural land to foreigners, on July 3 LFMI released a press release urging the parliament not to vote down the transition period. The transitional period to agricultural land sales, LFMI argued, would postpone already protracted agricultural reforms, hinder economic development in Lithuania and slow down the process of integration into the European Union.

Company law

When preparing a draft law on companies, the Ministry of Economy included the following proposals by LFMI: restrictions on the number of incorporators and shareholders and the size of corporate lending were removed, a diversity of the forms of voting was laid down, and a restriction of distribution of premiums and bonuses was lifted.

As the Ministry of Economy continued drafting the bill, LFMI once again submitted proposals for its revision. LFMI recommended to abandon prohibition for a company to mortgage corporate assets for lending purposes from its shareholders; to provide for a possibility to appeal to court a decision adopted by a general shareholders meeting not later than within thirty days following the date of adoption; to put more emphasis on the circumstance that voting is possible not only in writing, i.e. by means of filling in a general voting document, but also in other forms prescribed by the law; to juxtapose conflicting articles of the law with regard to the right of summoning up general shareholders meeting; and to eliminate the prohibition to transfer partially paid shares.

Deregulation

Building and Land Purchase. In order to enhance the efficiency of systems of registration of real estate, title to real estate and mortgage of real estate, LFMI launched a project "**Real Estate Registration and Mortgage Systems in Lithuania**." Within its framework, LFMI analyses the existing registration and mortgage systems of real estate in Lithuania and the procedures related to acquisition and mortgage of residential property, assesses the efficiency, advantages and disadvantages of these systems and the existing procedures, and evaluates the impact the Law on Activities of Real Estate and Mortgage Registers have on crediting. Moreover, LFMI makes a comparison between the system of registers in Lithuania and other possible systems and formulates proposals, which, if implemented, would facilitate the evolution of systems of property registration and mortgage into viable, safe, efficient systems and would contribute to simplifying housing crediting procedures. The project is scheduled for completion next February.

Civil Code. Public authorities continue to make efforts to regulate corporate interrelations demonstrating distrust in the legal acts which were developed by themselves and are already regulating these relations. When the Ministry of Economy elaborated a draft law on prevention of delays of payments in commercial transactions, LFMI noted that the new draft regulates issues already regulated by the Civil Code. So a question arises whether a separate regulation of interest payment is needed at all that would be enforced under this new law. The explanatory note justifies the necessity to have an individual law on payments in commercial transactions by EU requirements and a specific Directive 2000/35/EEC that provides for a detailed computation procedure of interest on delayed payments. LFMI underlined, however, that, regardless of this circumstance, not very precise requirements of the said Directive have been transferred into the draft law and thus the goals of harmonisation of EU and Lithuanian laws will not be achieved. At present debates on the prepared bill are ongoing in the parliament.

Education

LFMI continues a project "Building a Sound Voucher Funding System in Higher Education" with a goal to promote a funding reform in higher education based on the voucher principle, to provide independent expert input to the policy making process and to increase public awareness of the need and essence of the reform. On July 3, LFMI released a press release criticising the amendments to the Law on Higher Education adopted by the parliament. LFMI claimed that the implementation of these amendments pushed the higher education system into an even greater deadlock and would raise misleading expectations for people planning to study in higher educational establishments. According to these amendments, changes made to the Law on Higher Education earlier this year started to be enforced as from 1 September 2002, whereby a universal tuition fee of 1.000 litas was introduced in all higher educational establishments the remaining costs of studies being covered by the state. Higher schools are prohibited to enrol students who would cover the total price of studies at their own expense.

LFMI's policy analysts also submitted comments and proposals on a draft of government decree regulating issuance, administration and repayment of loans extended to students by the state.

After submission to the parliament, LFMI analysed the revised draft law on education and submitted its proposals on the remainder defective provisions of the bill. LFMI first submitted proposals on this law last January to the Ministry of Education and Science which approved of a number of LFMI recommendations. Nevertheless, the bill still contains quite a few faulty provisions which LFMI urged to revise.

Energy sector

When the parliament debated a draft law on the national energy strategy, LFMI's policy analysts took part in the hearings.

Welcoming the proposed direction of the strategy to liberalise the energy sector and the bulk of energy enterprises, LFMI submitted comments and recommendations on how to the energy sector could be deregulated, privatised and opened for international competition in a more consistent, customer- and market-friendly way.

Health care

As a follow-up to earlier activities in the area of health care reform, LFMI analysed draft provisions of the national pharmaceuticals policy and submitted comments to the parliament. As the first step, LFMI proposes to lay down in the document how the current inefficient policy of pharmaceuticals and health care could be amended so as to make it acceptable to the people, while consideration of health care problems would avail of more constructive measures than the reshuffle of health care ministers, redistribution of health care budget or additional funding dished out for "putting out the fires" in the health care system. Only then will it be possible to formulate the key principles of the reform and to draft provisions of the national pharmaceuticals policy on their basis. Until this is done, LFMI thinks, the parliament should reject the currently discussed draft provisions of the national pharmaceuticals policy.

LFMI analysed draft amendments to the law on health insurance and proposed shortening the list of people covered by state insurance; linking the size of health insurance contribution of self-employed people to the income they receive; toughening the financial accountability of the sate Patient's Funds, etc. LFMI believes that the implementation of these recommendations would contribute to the improvement of the health insurance system.

Proposals with regard to strategic trends of pharmaceutical activities and control thereof have also been submitted to a working group at the Office of the President which was set up for drafting strategic provisions for pharmaceutical activities and control (LFMI's Vice President G. Steponaviciene participates in this group).

Housing financing policy

As a follow-up to previous activities in the area of housing financing policy, on July 5th LFMI hosted a round table discussion on housing financing and the expediency of contractual savings system. Representatives of public authorities, financial sector and specialists of this field discussed the currently proposed contractual savings model to be launched in Lithuania following the suit of the so-called Bausparkassen system adopted in western countries. The discussion revolved around a draft law on savings for housing and housing financing which had been drafted in line with the principles of the Bausparkassen system. Papers on the problems of this system were delivered by Douglas B. Diamond, consultant of the Project on Housing in Lithuania; Artur Ploksto, member of the parliamentary committee on budget and finance; and Andrius Bogdanovicius, LFMI's policy analyst. Back in summer of this year, LFMI conducted an analysis on the contractual savings system and described the principles of the proposed model and overviewed the global practice. LFMI provided conspicuous conclusions on the forecasted costs for the public, the benefit for individual groups, the impact on the financial and housing market. According to LFMI's policy analysts, the most important goals established for this system would not be achieved, while its implementation would result in sizeable public costs and would have a negative impact on the market.

Having made an in-depth analysis into the said draft law on savings for housing and housing financing, LFMI submitted comments to public authorities on the expediency of the law. LFMI thinks that the implementation of the contractual savings scheme would not bring the desirable results and would, instead, become a burden on the state budget. Therefore, this idea should be abandoned altogether, while the hearing of the draft law should be halted until a comparative analysis on various housing financing instruments has been made and the National Housing Strategy has been drafted. Nevertheless, if it were decided to go ahead with the contractual savings model in Lithuania, LFMI's policy analysts submitted specific recommendations on how to revise the draft law.

LFMI has also analysed a draft law on mortgage bonds and mortgage lending which would regulate a new housing financing instrument – mortgage lending system. LFMI welcomes the proposal to introduce the mortgage lending system in Lithuania; however, the policy analysts underlined a number of shortcomings of the bill. First, the possibility to provide mortgage lending services and to issue mortgage bonds is limited only to credit institutions. Second, restrictions are provided for that would be imposed on credit beneficiaries and the utilisation of the credit. Third, too strict requirement is laid down with regard to the value proportion of the size of the credit secured by mortgage and mortgaged property. LFMI believes that these provisions of the bill would inevitably bring about stagnation of the market of mortgage bonds and low liquidity and would artificially narrow the circle of providers and users of mortgage credits. LFMI proposed to soften the said restrictions and thus create more favourable conditions for mortgage lending, a more flexible and more suitable model for Lithuanian (as compared with the contractual savings system).

In a press conference, September 30, LFMI's policy analysts highlighted once again the weaknesses of the contractual savings system and the negative results it would have on Lithuania. They also presented the advantages of the mortgage lending system and recommendations on the improvement of its regulation. LFMI's policy analysts stressed that introduction of the contractual savings model would prevent the adoption of a much more efficient system in Lithuania requiring no public expenditure – mortgage lending system.

Drawing on the results of the poll conducted from July 9 to 24, 2002 (2.998 households were polled), LFMI carried out a survey of Lithuanian households. The aim of this survey was to analyse Lithuanian households' income and expenditure, expectations regarding changes in their economic situation, expenditure priorities, housing conditions, willingness and efforts to improve housing conditions as well as attitudes towards commercial loans and state housing policy. The findings of the survey will be disseminated in the coming month.

LFMI believes that these activities will contribute to ensuring better conditions for the financial and housing market, as well as to enhancing the efficiency and expediency of the forms of state support.

Information technologies and telecommunications

One of major activities by LFMI in this field was its contribution to drafting amendments to the Law on Telecommunications which was adopted on July 5, 2002. LFMI's policy analysts took an active part in a working group set up to draft the law. At a later stage they presented the problems of this law to public authorities – Office of the President, the parliament, foreign experts and the public. From the very beginning of activities of the working group, LFMI proposed orienting towards a new package of EU directives, but this proposal was turned down. However, some of LFMI's proposals on the reduction of the scope and toughness of regulation of market players were approved.

LFMI highlighted the key problems of the then draft. These were: legal instability, administrative regulation of prices, non-transparent distribution of resources, possibility to protect state service providers, and insufficiently defined regulation of universal services in the law. During further discussions of the working group note was taken of several LFMI's proposals. Unfortunately, the following key proposals by LFMI were not included: the financing of universal services from the budget, the elimination of penalties from turnover and the reduction of operators' obligations to submit information to the intelligence services.

LFMI has also analysed draft regulations on provision of general mobile telephone communications services. The policy analysts pointed out that the draft regulations contain provisions which go beyond the scope of minimal regulation. LFMI suggested making an essential revision of the document by scrapping unnecessary or unjustified regulations and embedding in the provisions a possibility for a service provider and a customer to define their mutual relations by a contract.

Upon request of the World Bank, LFMI's policy analysts submitted comments on the World Bank's conclusions on business conditions in Lithuania in the context of knowledge economy. LFMI's Vice-president G. Steponaviciene also participated in a discussion held by the World Bank Mission on conditions for knowledge economy in Lithuania and delivered a presentation on preconditions of the development of innovations in the country.

NGO legislation

LFMI analysed a draft order drawn up by the Ministry of Finance on the forms and terms for submitting annual reports by support providers and support receivers. It contains a provision stipulating that the forms of reports are to be established by the central tax administrator rather than laid down in the order itself. More than that, the drafters intended to set the procedure for submitting reports requiring support providers and receivers to identify for which areas and public aims the support was utilised. LFMI noted that such a provision would result in many inconveniences and confusion for supporters of non-government organisations and the organisations themselves. The Ministry of Finance only partially consulted the opinion of LFMI in that under the established procedure reports will have to be submitted for 2003 and successive years, whereas reports for 2002 could be submitted in a free (or recommended) rather than obligatory form. LFMI thinks that companies and non-profit organisations will find it difficult to provide this information as they did not know beforehand about the types of information they would have to provide and the ways of accumulation thereof. LFMI had already initiated changes in the regulation of reporting of charity and support: according to the amended Law on Charity and Support, organisations are now required to report once a year to one institution instead of four times a year to two institutions.

Pension reform

In September the Government approved of a revised draft law on pension reform which is currently under the parliamentary debates. According to the bill, 2.5 percent of the social security contribution will be diverted for accumulation in a private pension fund, the employer's contribution paid to the state social insurance fund being reduced accordingly. The contribution will be increased to 5.5 percent in 2007. It should be noted that a conceptual framework of pension reform was drafted and debated for quite a long time, then it was submitted to the Parliament and returned to the Government for revision. When the Parliament turned down the first draft law on pension reform, LFMI's policy analysts submitted policy recommendations to the Ministry of Social Affairs and Labour and the Parliament. LFMI proposed to lay down an alternative to accumulate private pensions not only in private pension funds but also in private insurance companies. LFMI also recommended retaining the right for all people, regardless of their age, to choose whether to accumulate the determined contribution privately or to leave it with the government-run system. Both proposals were incorporated in the revised bill. People will be allowed to choose were this contribution should be accumulated, i.e. if an individual is willing to remain in the government-run system, he will not be forced to move to the private pension system. This element will help preventing pension reform from discredit if, in mandatory case, workers were forced into a private pension system and received poorer returns that they expected. A voluntary aspect of the reform also prevents the government from assuming responsibility for private pensions as the system is not mandatory.

Property rights

LFMI is launching a new project "The Protection of Property Rights and State Economic Sanctions Policy" which is aimed at promoting development of an efficient protection system of property rights by means of identifying problems related to the concept of property laid down in the Lithuanian laws and submitting recommendations as to how better protect property rights in relations of imposing and enforcing proprietary sanctions. LFMI will implement this project together with the Human Studies Centre.

Public administration

Public Procurement. When the parliament was hearing a draft law on public procurement, LFMI submitted a package of policy proposals on broaden the definition of public procurement, since, in LFMI's opinion, it will be more expedient and beneficial to regulate more types of procurement in Lithuania in addition to the ones regulated in the EU (the EU strictly regulates part of public procurement (international procurement), while the EU institutions take part in the procuring process). LFMI also submitted recommendations on how to regulate public procurement more explicitly seeking transparency and efficiency in this area.

Ethics of public servants. At present, legal acts crucial for the public and state administration are being drafted which will lay down the rules of ethics of public servants and politicians. In order to ensure a successful drafting and adoption thereof, LFMI is conducting a public opinion survey on the ethics of politicians' behaviour and the efficient measures ensuring impeccable and ethical behaviour of politicians.

Social policy

LFMI has analysed a draft law on monetary social support and submitted comments to public authorities. According to LFMI, this law fails to integrate all forms of monetary support currently rendered in Lithuania. Moreover, despite that public authorities declare the need to establish a uniform criterion of income and property for allotting state support, the bill stipulates various criteria to be applied to different groups of society. LFMI has repeatedly called for rendering one integrated form of state monetary support that would be based on the only criterion – receiver's income and property.

Tax policy

LFMI's policy analysts continued analysing legal acts regulating taxes and actively participated in the Sunrise task force on taxation. The task force discussed secondary legislation of the laws on Income Tax, Value Added Tax, Private Income Tax and Excise Duty. When drafting final versions of legal acts, the Ministry of Finance included many proposals of the task force. It should be noted that the Ministry of Finance approves of the LFMI's proposal to adopt amendments to the Law on Tax Administration, whereby the Ministry of Finance would be entitled to interpret legal acts regulating taxes rather than the State Tax Inspectorate, currently performing this function.

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The Free Market is published by the Lithuanian Free Market Institute – an independent non-profit organisation established in 1990 to advance the ideas of individual freedom and responsibility, free market and limited government. Our motto is

If you don't create a free market, a black market will emerge

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LFMI pursues its mission by conducting research on key economic policy issues, developing conceptual reform packages, submitting policy recommendations at the legislative and executive levels, drafting and evaluating legislation, and launching public campaigns. LFMI's activities also include sociological surveys, publications, conferences, workshops, and lectures.

LFMI receives financial support from individuals, corporations and foundations. Devoted to the principles of private ownership, LFMI accepts no funds form the Lithuanian government.

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